

Report of the auditor-general to the North West provincial legislature and the council on the Kagisano Molopo Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Kagisano Molopo Local Municipality set out on pages xx to xx, which comprise of the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of Kagisano Molopo Local Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

Basis for qualified opinion

Property, plant and equipment

3. I was unable to obtain sufficient appropriate audit evidence for infrastructure and community assets included in property, plant and equipment due to the status of the accounting records and non-submission of information in support of this balance. I was unable to confirm these assets by alternative means. In addition, the municipality incorrectly classified assets that meets the criteria for investment property in terms of GRAP 16, *Investment property* as property, plant and equipment and incorrectly calculated the depreciation charged required by GRAP 17, *Property, plant and equipment* by using incorrect useful lives and residual values in the calculation. This resulted in property, plant and equipment being understated by R7 910 879, the depreciation expense being overstated by R10 370 144 and investment property being understated by R2 459 265. Consequently, I was unable to determine whether any further adjustment to property, plant and equipment of R443 713 179 as presented in the statement of financial position and disclosed in note 4 to the financial statements was necessary.

Irregular expenditure

4. Section 125 of the MFMA requires the disclosure of irregular expenditure incurred. The municipality made payments of R43 457 707 in contravention with the supply chain

management requirements which were not included in irregular expenditure disclosed. As the municipality did not quantify the full extent of the irregular expenditure, it was impracticable to determine the resultant understatement of irregular expenditure of R276 571 714 disclosed in note 43 to the financial statements.

Context for the opinion

5. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
6. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' Code of ethics for professional accountants (IESBA code) together with the ethical requirements that are relevant to my audit. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

8. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material losses

9. As disclosed in note 27 to the financial statements, material losses to the amount of R10 056 386 (2016: R3 614 927) were incurred as a result of significant impairment of debtors.

Material uncertainty relating to contingencies

10. As disclosed in note 34 of the financial statements the municipality has contingent liabilities amounting to R1 913 419 and contingent assets amounting to R5 972 427 which will only be confirmed after the occurrence of future events.

Restatement of corresponding figures

11. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of an error discovered during 30 June 2017 in the financial statements of the Kagisano Molopo Local Municipality at, and for the year ended 30 June 2017.

Unauthorised and fruitless and wasteful expenditure

12. As disclosed in the note 41 to the financial statements, unauthorised expenditure of R17 605 127 was incurred in the current year and the unauthorised expenditure of R101 151 349 in respect of prior years had not yet been dealt with in accordance with section 32 of the MFMA.
13. As disclosed in the note 42 to the financial statements, fruitless and wasteful expenditure of R41 243 was incurred in the current year and the fruitless and wasteful expenditure of R1 878 129 in respect of prior years had not yet been dealt with in accordance with section 32 of the MFMA.

Other matters

14. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

15. In terms of section 125(2) (e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirements did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Unaudited supplementary schedules

16. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited this schedules and, accordingly, I do not express an opinion thereon.

Responsibilities of the accounting officer for the financial statements

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA standards of GRAP and the requirements of the MFMA and the DoRA and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
18. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless there is an intention either to liquidate the municipality or to cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

19. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

Report on the audit of the annual performance report

Introduction and scope

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
22. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.



23. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2017:

Objectives	Pages in the annual performance report
Key performance area 2: Basic service delivery and infrastructure development	xx – xx
Key performance area 3: Local economic development and community services	xx – xx

24. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
25. I did not identify any material findings on the usefulness and reliability of the reported performance information for these objectives of the municipality.

Other matters

26. I draw attention to the matters below.

Achievement of planned targets

27. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year.

Adjustment of material misstatements

28. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of Key performance area 2: Basic service delivery and infrastructure development and Key performance area 3: Local economic development and community services. As management subsequently corrected these misstatements, I did not report any material findings on the usefulness and reliability of the reported performance information.

Report on audit of compliance with legislation

Introduction and scope

29. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
30. The material findings in respect of the compliance criteria for the applicable subject matters are as follows:

Budget

31. Reasonable steps were not taken to prevent unauthorised expenditure of R25 964 051, as disclosed in note 43 to the financial statements, in contravention of section 62(1)(d) of the



MFMA. The majority of the unauthorised expenditure was caused by overspending by vote 7 – Technical Services.

Financial statements

32. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Procurements and contract management

33. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements as proper record management was not in place to ensure that all the requested bidding documents was available.
34. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of by SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
35. Some of the quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
36. Sufficient appropriate audit evidence could not be obtained that quotations were only accepted from bidders whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
37. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Similar non-compliance was also reported in the prior year.
38. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2). Similar non-compliance was also reported in the prior year.
39. Some of contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding, in contravention of SCM regulation 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
40. Sufficient appropriate audit evidence could not be obtained that all extensions or modifications to contracts were approved by a properly delegated official, as required by SCM regulation 5.
41. Awards were made to providers whose directors or principal shareholders are in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore the provider failed to declare that he / she was in the service of the municipality, as required by SCM regulation 13(c).
42. Awards were made to providers whose directors or principal shareholders were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).
43. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) and the code of conduct for councillors issued in terms of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and the code of conduct for staff members issued in terms of the MSA.
44. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in

contravention of SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA and the code of conduct for staff members issued in terms of the MSA.

Expenditure management

45. Effective steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for opinion paragraph. The majority of the disclosed irregular expenditure was caused by not following competitive bidding process as required by SCM regulation 19(a). Irregular expenditure of R5 627 996 was incurred on construction of the selected key projects of Kgokgole community hall, Phaphosane community hall and Gamanyai and Tlakgameng high mast lights.
46. Effective steps were not taken to prevent fruitless and wasteful expenditure of R41 243, as disclosed in note 43 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest paid on Eskom invoices.

Revenue management

47. Accounts for municipal tax and charges for municipal services were not prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.

Consequence management

48. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) and (b) of the MFMA.
49. Allegations of financial misconduct against the accounting officer relating to prior year unauthorised, irregular and fruitless and wasteful expenditure were not always investigated, as required by Disciplinary regulations for senior managers 5(3) and section 171(4) of MFMA.

Human resource management

50. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the MSA.

Other information

51. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report thereon and those selected objectives presented in the annual performance report that have been specifically reported on in the auditor's report.
52. My opinion and findings do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
53. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected objectives presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
54. I did not receive the other information prior to the date of the auditor's report. When I do receive this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to re-issue my auditor's report amended as appropriate.

Internal control deficiencies

55. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion and the findings on compliance with legislation included in this report.
- The leadership did not adequately exercise appropriate oversight over financial and compliance monitoring and related internal controls. Policies and procedures did not adequately guide financial and compliance activities. Furthermore, material misstatements were identified in the financial statements and performance reports which were not prevented by internal policies and controls.
 - Management's internal controls and processes over the preparation and presentation of financial statements and performance information were not adequate to ensure that the financial statements were free from material misstatements. Non-compliance with laws and regulations could have been prevented had compliance been properly reviewed and monitored and control measures implemented. Policies and procedures have not always adequately guided financial activities as well as action plans to address prior year audit findings.
 - The risks identified during the risk assessment process relating to financial reporting and compliance with laws and regulations were not adequately monitored by management resulting in weaknesses in the internal control environment. The messages and recommendations from the audit committee and internal audit did not yield the required results as material misstatements and findings were identified in the financial statements and the performance report submitted for audit as well as material non-compliance with legislation.

Auditor General

Potchefstroom

30 November 2017



Auditing to build public confidence

Annexure – Auditor-general’s responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected objectives and on the municipality’s compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in the auditor’s report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control.
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
 - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on Kagisano Molopo Local Municipality’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause the municipality to cease to continue as a going concern.
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and here applicable, related safeguards.

